1975 Annual Report

INTERNATIONAL DAIRY QUEEN, INC.

HARRIS COOPER
President

WILLIAM B. McKINSTRY
Chairman of the Board

Dairy Queen *

TO OUR SHAREHOLDERS:

Your Company is engaged in the business of developing, licensing, and servicing a system of retail stores which offer a limited menu of food items, including soft-serve dairy products, hamburgers and beverages which are marketed under the "Dairy Queen", "Brazier" and "Mr. Misty" trademarks. Since the opening of the first "Dairy Queen" store in 1940, the system has expanded on a national and international basis and at November 30, 1975, was comprised of 4,675 stores, of which 4,240 stores were located in the United States, 360 stores in Canada, and 75 stores in other countries. Of the 4,675 stores, 2,252 were franchised by the Company, 9 were operated by the Company, and 2,414 were subfranchised by licensed territorial operators.

The Company is one of 102 approved manufacturers of "Dairy Queen" mix. In addition, the Company sells equipment directly to stores and food and other products manufactured by independent manufacturers directly to warehouses. The Company and its subsidiaries also provide equipment financing and real estate leasing and financing services to store owners.

During fiscal 1975, your Company enjoyed continued growth in revenues and earnings. Earnings for 1975 increased to $1,008,168 from $817,533 in 1974, an increase of 23.3%. These increases were due primarily to the increased sales by stores franchised by the Company and subfranchised by territorial operators, and in your management's opinion, reflect the Company's continuing efforts to increase the sales and profitability of individual stores. These increases were achieved even though there was a decrease in equipment sales and financing income as a result of a lesser number of new stores opened. The decrease in new store openings is a result of our increasing efforts in screening new franchisees and store locations in order to better insure that each new store will contribute to the long-term growth of the Company and the "Dairy Queen" system. Revenues for 1975 increased to $54,501,516 from $52,641,072 in 1974.

*Reg. U.S. Pat. Off. Am. D.Q. Corp.

We believe it would be helpful to our shareholders in putting these results into perspective to provide a more detailed analysis of the statement of income and retained earnings for fiscal 1975 compared to fiscal 1974 and fiscal 1974 compared to fiscal 1973 (see Financial Summary). Results of operations during this period reflected rapidly changing economic conditions, including abnormal increases in the rate of inflation, government controls on wages and prices, and frequent fluctuations in the prime interest rate.

Net Sales and Cost of Sales. The increases in 1975 resulted primarily from increases in the number of units of food and supplies purchased and sold, offset to a significant extent by a reduction in equipment sales due to a reduction in the number of new stores opened. The increases in 1974 resulted primarily from increases in prices due to inflation.

Service Fees. The increase in service fees (revenues received from stores franchised by the Company and from stores subfranchised by territorial operators) in 1975 resulted primarily from increases in unit sales by stores, and to a lesser extent, service fees paid by stores opened in 1974 and 1975. The increase in 1974 resulted primarily from increases in prices due to inflation and, to a lesser extent, from increases in unit sales by stores.

Franchise Sales and Other Fees. The increase in 1975 resulted primarily from increases in the miscellaneous categories included under "Other Fees" and the increase in 1974 resulted primarily from fees generated in connection with new store openings.

Real Estate Rentals—Revenue and Expense. The increases in 1975 and 1974 resulted primarily from the cumulative effect of new leases and subleases entered into in connection with new store openings.

Other Revenue. The decrease in 1975 resulted primarily from a reduction in financing income due to a decrease in the number of equipment finance contracts entered into during the year. The decrease in 1974 reflected both the absence of a gain on the disposal of warehouse operations during fiscal 1973 and a reduction in insurance commissions due to a less favorable claim experience.

Selling, General and Administrative. The increases in 1975 and 1974 reflected increased activity in many areas of the Company's business and higher costs of operation due to inflation. These increases were, however, offset to a significant extent by a cost control program implemented by management during the first portion of fiscal 1974.

Interest. The decrease in 1975 and the increase in 1974 resulted primarily from fluctuations in the prime interest rate.

Income Taxes. The provision for income taxes as a percentage of income before income tax increased from 27.2% in 1973 and 1974 to 37.1% in 1975. The reasons for the increase are set forth in Note 4 of the Notes to Consolidated Financial Statements.

On balance, management considers fiscal 1975 to have been a good year for your Company, with significant progress being made in building a solid base which should support the Company's and the "Dairy Queen" system's continued growth and profitability.

Sincerely,
INTERNATIONAL DAIRY QUEEN, INC.

Harris Cooper
HARRIS COOPER
President

William B. McKinstry
WILLIAM B. McKINSTRY
Chairman of the Board

INTERNATIONAL DAIRY QUEEN, INC.

CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS
Years ended November 30, 1975 and 1974

	1975	1974
Revenues:		
Net sales	**$36,827,010**	$36,072,993
Service fees	**9,211,853**	8,431,067
Franchise sales and other fees	**2,925,795**	2,716,494
Real estate rentals	**4,065,153**	3,845,681
Other	**1,471,705**	1,574,837
	54,501,516	52,641,072
Costs and expenses:		
Cost of sales	**33,394,432**	32,357,715
Expenses applicable to real estate rentals	**3,564,332**	3,470,081
Selling, general and administrative	**13,671,671**	12,908,304
Interest	**2,267,913**	2,782,439
	52,898,348	51,518,539
Income before income taxes	**1,603,168**	1,122,533
Provision for income taxes (Note 4)	**595,000**	305,000
Net income	**1,008,168**	817,533
Retained earnings at beginning of year	**4,250,022**	3,459,443
	5,258,190	4,276,976
Dividends paid on special preference stock	**29,478**	26,954
Retained earnings at end of year	**$ 5,228,712**	$ 4,250,022
Earnings per share (Note 1)	**$ .17**	$ .15

See accompanying notes.

INTERNATIONAL DAIRY QUEEN, INC.

CONSOLIDATED BALANCE SHEET
November 30, 1975 and 1974

ASSETS	1975	1974
Current assets:		
Cash (Note 5)	$ 4,729,813	$ 3,796,544
Notes and accounts receivable, less allowance of $566,721 for doubtful amounts (1974—$803,674)	5,763,373	7,006,447
Finance and lease contracts, less unearned income of $518,251 (1974—$722,492) (Note 5)	738,002	688,654
Inventories (Note 2)	1,448,062	1,601,083
Prepaid expenses	468,165	480,277
Total current assets	13,147,415	13,573,005
Other assets:		
Notes receivable, less allowance of $253,972 for doubtful notes (1974—$136,399)	1,444,657	1,847,771
Intangibles, net of amortization	366,129	344,065
Miscellaneous	468,176	449,733
Total other assets	2,278,962	2,641,569
Other revenue producing assets:		
Finance and lease contracts, less unearned income of $874,514 (1974—$1,571,074) (Note 5)	3,044,925	4,184,930
Rental properties, net (Notes 3 and 5)—		
Real estate	4,324,370	3,073,576
Equipment	1,441,920	1,429,898
Franchise rights and service contracts, at cost less accumulated amortization of $516,353 (1974—$388,068) (Note 5)	17,539,428	17,651,316
Total other revenue producing assets	26,350,643	26,339,720
Other property, plant and equipment, net (Notes 3 and 5)	1,489,227	1,155,380
	$43,266,247	$43,709,674

See accompanying notes.

LIABILITIES AND STOCKHOLDERS' EQUITY	1975	1974
Current liabilities:		
Notes payable, unsecured	**$ 493,000**	$ 505,000
Drafts and accounts payable	**6,035,144**	4,836,253
Accrued interest and other liabilities	**1,284,580**	1,119,007
Income taxes	**123,287**	160,535
Current maturities of other long-term debt	**3,074,187**	2,715,246
Total current liabilities	**11,010,198**	9,336,041
Deferred franchise fees	**283,922**	459,732
Deferred income taxes	**335,000**	—
Other long-term debt (Note 5)	**18,217,489**	21,502,834
Subordinated convertible debentures (Note 5)	**2,000,000**	2,000,000
Commitments and contingencies (Note 6)		
Stockholders' equity (Notes 7 and 8):		
Special preference stock, $10 par value; authorized 1,000,000 shares:		
Special 4% cumulative preferred stock, Series A; authorized 450,000 shares, issued and outstanding 72,874 shares	**728,740**	728,740
Special 7% cumulative preferred stock, Series B; authorized 60,000 shares, issued and outstanding 11,412 shares (1974—5,706 shares)	**114,120**	57,060
Common stock, $1 par value; authorized 10,000,000 shares, issued 5,145,318 shares	**5,145,318**	5,145,318
Paid-in capital	**511,474**	538,653
Retained earnings (Note 5)	**5,228,712**	4,250,022
	11,728,364	10,719,793
Less cost of 91,822 common treasury shares	**308,726**	308,726
Total stockholders' equity	**11,419,638**	10,411,067
	$43,266,247	$43,709,674

INTERNATIONAL DAIRY QUEEN, INC.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
Years ended November 30, 1975 and 1974

	1975	1974
Source of working capital:		
Net income	**$ 1,008,168**	$ 817,533
Items not involving working capital:		
Depreciation	**558,908**	472,646
Amortization of franchise rights and other intangibles	**316,202**	260,720
Deferred income taxes	**335,000**	—
Other, net	**53,021**	107,691
Total from operations	**2,271,299**	1,658,590
Additions to other long-term debt	**1,826,135**	3,549,630
Reduction in finance and lease contracts	**2,360,419**	2,685,158
Proceeds of property and equipment disposals	**1,010,157**	785,574
Issuance of common and special preference stock	**57,060**	77,060
Additions to deferred franchise fees, net of refunds	**33,500**	27,950
Decrease in notes receivable due after one year	**403,114**	140,182
	7,961,684	8,924,144
Disposition of working capital:		
Reduction in other long-term debt	**5,111,480**	3,469,296
Additions to—		
Finance and lease contracts	**1,220,414**	2,616,336
Rental properties	**2,338,468**	1,669,296
Franchise rights and service contracts	**111,152**	779,668
Other property, plant and equipment	**841,853**	376,785
Deferred costs relating to deferred franchise fees	**245,669**	313,224
Other, net	**192,395**	(5,881)
	10,061,431	9,218,724
Increase (decrease) in working capital	**$(2,099,747)**	$(294,580)
Analysis of increase (decrease) in working capital:		
Cash	**$ 933,269**	$ 177,126
Notes and accounts receivable	**(1,243,074)**	1,429,425
Finance and lease contracts	**49,348**	(22,107)
Inventories	**(153,021)**	(805,031)
Prepaid expenses	**(12,112)**	(110,665)
Notes payable	**12,000**	(505,000)
Drafts and accounts payable	**(1,198,891)**	(248,194)
Accrued interest and other liabilities	**(165,573)**	6,390
Income taxes	**37,248**	89,187
Current maturities of other long-term debt	**(358,941)**	(305,711)
Increase (decrease) in working capital	**$(2,099,747)**	$(294,580)

See accompanying notes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
November 30, 1975 and 1974

1. Summary of significant accounting policies

Consolidation policy and basis of presentation —

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly-owned. The investment in a foreign joint venture, which is not material to the consolidated financial statements, is accounted for on the equity method. All significant intercompany transactions are eliminated in consolidation.

The financial statements of foreign subsidiaries, principally Canadian, and the joint venture are translated into U.S. dollars based on (1) current exchange rates for current assets and liabilities, (2) historical exchange rates for noncurrent assets and liabilities and stockholders' equity, and (3) average exchange rates for revenues, costs and expenses (other than depreciation and amortization) and income taxes. Exchange adjustments, which have not been material, are included in operations. In October 1975, the Financial Accounting Standards Board adopted Statement No. 8 on accounting for the translation of foreign currency financial statements, which will require certain changes, not expected to have a material effect, in the method currently used by the Company.

In fiscal 1975 the Company formalized its vacation policy to provide for vesting of vacation rights earned. Accordingly, the Company has provided for approximately $137,000 of vacation pay in fiscal 1975.

Certain reclassifications have been made in the 1974 financial statements to make them comparable with the presentations for 1975.

Research and development costs —

In accordance with Statement No. 2 of the Financial Accounting Standards Board, the Company adopted in 1974, with retroactive application, the policy of expensing as incurred all research and development costs. Such costs were previously deferred and amortized over periods ranging from 3 to 5 years.

Depreciation and amortization —

Depreciation and amortization of rental properties and other property, plant and equipment are provided principally on the straight-line method over estimated useful lives of 15 to 40 years for buildings, 5 to 10 years for equipment and over the remaining terms of the leases for leasehold improvements.

The Company believes there has been no diminution in the value of franchise rights and service contracts since the dates of their acquisition and follows a policy of non-amortization of franchise rights and service contracts acquired prior to November 1970. The cost of franchise rights and service contracts acquired subsequent to October 31, 1970 (approximately $5,000,000) is being amortized generally over 40 years on a straight-line basis.

Intangibles include trademarks, trade names and goodwill. Trademarks and trade names are amortized over 5 years and goodwill was amortized over 40 years prior to fiscal 1975 and over 10 years commencing in fiscal 1975. The change in estimated useful life did not have a material effect on the consolidated financial statements.

Revenue recognition —

The Company recognizes revenues from initial store franchise fees when the store is opened. Direct costs incurred prior to store openings are deferred until the revenue is recognized. Deferred franchise fees are net of deferred costs of $78,578 and $337,268 at November 30, 1975 and 1974, respectively.

The Company leases equipment under noncancellable leases for periods ranging from 3 to 10 years. The leases provide for substantial recovery of the Company's investment in the leased equipment during the initial term of the lease and are accounted for under the financing method. Estimated residual values of leased equipment in the amount of $263,000 and $349,000 at November 30, 1975 and 1974, respectively, are included with finance and lease contracts. Equipment is also leased on a short-term basis and the rentals are recorded in income as earned.

Income taxes —

The Company and its U.S. subsidiaries file a consolidated federal income tax return. No provision is made for taxes which would be payable with respect to undistributed earnings of the Company's foreign subsidiaries, since it is the Company's intention to utilize such earnings to finance continued expansion outside the United States. The unremitted earnings which have been, or are intended to be, permanently reinvested aggregated approximately $800,000 at November 30, 1975.

Certain revenues and expenses are recognized in different periods in determination of book and taxable income, and the Company follows the practice of providing deferred income taxes on the net change method for these timing differences.

Investment tax credits are accounted for on the flow-through method as a reduction of income tax expense.

Earnings per share —

Earnings per share amounts are based on the weighted average number of common and dilutive common equivalent shares outstanding during each year and are after recognition of dividend requirements on the special preference stock and before interest deductions, net of income taxes, on the subordinated convertible debentures. Common share equivalents consist of shares issuable upon exercise of stock options and conversion of subordinated convertible debentures and special preference stock. Assumed conversion of other convertible debt would be antidilutive in both years. The weighted average number of common and common equivalent shares used in the

computations for the years ended November 30, 1975 and 1974 were 6,392,584 and 6,389,201, respectively.

2. Inventories

Inventories at lower of cost (first-in, first-out) or market (replacement cost or net realizable value, as appropriate) consist of the following:

	1975	1974
Store equipment	$1,192,382	$1,120,584
Merchandise	255,680	446,049
Store properties held for resale	—	34,450
	$1,448,062	$1,601,083

3. Rental properties and other property, plant and equipment

	1975	1974
Rental properties:		
Real estate, at cost:		
Land	$1,919,282	$1,314,869
Buildings	2,431,922	1,579,974
Leasehold improvements	316,930	285,025
Construction in progress	190,374	275,341
	4,858,508	3,455,209
Less accumulated depreciation	534,138	381,633
	$4,324,370	$3,073,576
Equipment, at cost	$1,784,152	$1,673,936
Less accumulated depreciation	342,232	244,038
	$1,441,920	$1,429,898
Other property, plant and equipment, at cost:		
Land	$ 162,449	$ 112,681
Buildings	226,386	269,222
Equipment	1,341,229	1,269,773
Leasehold improvements	388,335	179,835
Construction in progress	182,207	75,430
	2,300,606	1,906,941
Less accumulated depreciation	811,379	751,561
	$1,489,227	$1,155,380

4. Income taxes

The provision for income taxes in 1975 consists of current foreign and state income taxes of $235,000 and $25,000, respectively, and deferred income taxes (principally federal) of $335,000. The provision for income taxes in 1974 consists of current foreign income taxes of $285,000 and deferred state income taxes of $20,000. The provision for income taxes has been reduced by approximately $133,000 and $25,000 of investment tax credits in 1975 and 1974, respectively.

The deferred income taxes result principally from (a) differences in timing of revenue recognition from initial store franchise fees, (b) deduction of related direct costs and certain other franchise development costs as incurred for income tax purposes, (c) reporting of equipment leases on the operating method for income tax purposes which have been recorded on the financing method on the books, (d) the excess of tax over book depreciation and (e) provisions for expenses of store closings not deductible for income tax purposes until incurred.

At November 30, 1975, the Company has approximately $400,000 of net operating losses available to offset domestic taxable income of future years and approximately $230,000 of investment tax credit carryovers. To the extent these losses and credits are utilized for income tax purposes, there will be no effect on net income as the tax effect will be credited to deferred income taxes. One of the Company's Canadian subsidiaries has approximately $155,000 of unused net operating losses. To the extent these losses are utilized, the tax effect will be recognized as a credit to income.

The following is a reconciliation of differences between the federal statutory income tax rate of 48% and the consolidated effective tax rate:

	1975	1974
Federal statutory rate	48.0%	48.0%
Amortization and deduction of franchise rights for income tax purposes which are not being amortized for financial accounting purposes	(9.3)	(13.7)
Losses of foreign subsidaries and joint ventures not resulting in income tax benefit	4.1	4.3
Forgiveness of indebtedness from consolidated foreign subsidiary	—	(16.7)
Foreign income taxes, rate differences	1.6	3.8
Investment tax credits	(8.3)	(2.2)
Other, net	1.0	3.7
Consolidated effective tax rate	37.1%	27.2%

5. Long-term debt and short-term borrowing arrangements

The subordinated convertible debentures bear interest at prime rate plus ½% (8% and 11% at November 30,1975 and 1974, respectively), mature in 1981 and are convertible at the option of the holders into shares of common stock at the rate of $1.50 per share at any time prior to maturity. The debenture purchase agreement originally provided for conversion into common stock any time prior to March 1, 1976 and required the Company to pre-pay annually $400,000 principal amount commencing March 1, 1977. In fiscal 1975, the agreement was amended to extend the conversion privilege to March 1, 1981 and to waive the prepayment requirement.

Other long-term debt is summarized as follows:

	1975	1974
Note payable to bank under revolving credit agreement, bearing interest at prime rate plus ½% (8% at November 30, 1975 and 11% at November 30, 1974) maturing December 31, 1976	**$10,000,000**	$10,000,000
Other bank indebtedness, secured by finance and lease contracts and equipment, maturing at various dates through 1980—		
At beginning of month prime rate plus 1¾% (9½% at November 30, 1975 and 13% at November 30, 1974). (Current maturities—$904,155 in 1975 and $1,217,770 in 1974.)	**3,709,419**	6,083,390
At 127% of prime rate (9⅞% at November 30, 1975). (Current maturities $204,954.)	**834,264**	—
Notes payable, secured by franchise rights and service contracts of $9,538,000 at November 30, 1975 and $10,366,000 at November 30, 1974, at interest rates ranging from 4% to 8% (4% to 11% at November 30, 1974) and maturing at various dates through 1997. (Current maturities—$1,279,777 in 1975 and $1,091,591 in 1974.)	**4,506,064**	5,594,918
Real estate mortgages and contracts payable, at interest rates ranging from 6% to 12¼% and maturing at various dates through 1987. (Current maturities —$237,662 in 1975 and $169,691 in 1974.)	**1,636,695**	1,140,117
Notes payable, unsecured, at interest rates ranging from 6% to 8% (6% to 11% at November 30, 1974) and maturing at various dates through 1983 (Current maturities—$99,478 in 1975 and $119,111 in 1974.)	**190,494**	870,550
Equipment contracts payable, at interest rates up to 14% and maturing at various dates through 1980. (Current maturities—$62,861 in 1975 and $55,023 in 1974.)	**129,440**	181,745
6% notes payable, maturing in 1976 and payable in cash or in special preference stock, $10 par value. (Current maturities—$285,300 in 1975 and $62,060 in 1974.)	**285,300**	347,360
	21,291,676	24,218,080
Less current maturities of other long-term debt	**3,074,187**	2,715,246
Other long-term debt due after one year	**$18,217,489**	$21,502,834

The Company entered into a loan agreement with two banks in 1973, which, as amended, currently provides for a $10,000,000 revolving line of credit through December 31, 1976. The due date may be further extended from time to time by mutual consent of the parties. The agreement provides for interest at ½% per annum in excess of prime interest rate on the outstanding balance and for a commitment fee of ½% of the unused credit. The agreement also contains provisions, among others, limiting additional indebtedness and commitments under lease agreements, and restricting the Company from redeeming its capital stock or paying dividends in excess of an amount equal to 25% of the cumulative aggregate of its earnings subsequent to May 31, 1972. At November 30, 1975, consolidated retained earnings of $4,457,617 are restricted under the provisions of this loan agreement. The loans are secured by the outstanding stock of the Company's subsidiaries and the stock of any new subsidiaries is to be pledged as collateral. In connection with the loan agreement, the Company has informally agreed to maintain an average annual compensating balance, not restricted as to withdrawal, of approximately 15% of the line.

The Company's revolving credit agreement provided for borrowings of up to $3,000,000 on a short-term basis from February 7, 1974 through August 1, 1974 and up to $2,500,000 from January 15, 1975 through September 30, 1975 at the same terms as the original agreement. During the period from January 15, 1975 to September 30, 1975 the Company borrowed a maximum of $2,500,000 on a short-term basis. The approximate average daily amount of such borrowings was $1,600,000 during this period and the weighted average interest rate, giving effect to the fee for the unused commitment, was approximately 8½%. The Company borrowed $3,000,000 under this agreement for a period of 58 days during 1974. The weighted average interest rate on these borrowings, after giving effect to the fee for the unused commitment, was approximately 12¾%.

Dairy Queen Financial, Inc. ("Financial"), a wholly-owned subsidiary, has a revolving credit and security agreement with the Northwestern National Bank of Minneapolis as lead bank which, as amended, provides for an aggregate commitment of $8,000,000 through December 31, 1976. The agreement provides that loans are to be secured by the assignment of leases or finance contracts and that monthly principal payments be made over a period not to exceed 5 years based upon the monthly reductions in principal amount of the assigned contracts or the monthly depreciation provided on equipment leases that are assigned as security. The agreement further provides for interest at the greater of 1¾% per annum in excess of the prime interest rate or 7¾% per annum (127% of the prime rate for borrowings after October 3, 1975); for a commitment fee of ½% per annum on the daily average of the unused amount of the total commitment; and for a service fee of ¼% per annum on the amount of all advances. The agreement also contains provisions, among others, limiting further indebtedness of Financial, requir-

ing the Company to guarantee all obligations of Financial and requiring that the ratio of consolidated indebtedness to consolidated net worth of the Company (as defined) not to exceed a specified limit.

In November, 1975, the Company filed a registration statement with the Securities and Exchange Commission, which became effective on January 7, 1976, for the sale of up to $3,000,000 of unsecured 10¼% subordinated capital notes. The notes, which will mature in 1986, will be senior to the Company's subordinated convertible debentures but will be subordinated to bank debt and other institutional indebtedness. The notes are to be issued under an indenture which, with certain exceptions, limits amounts available for dividends and redemption of capital stock to 25% of the cumulative aggregate of earnings subsequent to November 30, 1975 and contains certain other covenants and restrictions.

Aggregate maturities of subordinated convertible debentures and other long-term debt at November 30, 1975 (which includes maturity of the $10,000,000 revolving credit note in fiscal 1977) are approximately as follows:

1976	$ 3,074,000
1977	12,316,000
1978	1,665,000
1979	1,348,000
1980	433,000
Thereafter	4,456,000

6. Commitments and contingencies

The Company and its subsidiaries have leases for Dairy Queen retail stores, warehousing and administrative facilities and equipment with varying terms up to twenty-five years. Certain of the leased properties are subleased to franchise operators under noncancellable subleases with rentals generally equal to or greater than rentals payable on the prime leases. The leases and subleases generally require the lessee to pay property taxes, maintenance and insurance; and many of the leases provide for one or more renewal options. In addition, the Company receives rental income aggregating approximately $250,000 annually from leasing Company-owned real estate to franchise operators under noncancellable leases with terms up to twenty-five years.

The approximate amounts of rental expense charged to operations (exclusive of taxes, insurance and maintenance) and rental income are summarized below. Rentals computed on bases other than the lapse of time are nominal.

	Non-capitalized financing leases		Other leases	
	1975	1974	**1975**	1974
Rental expense	**$2,831,000**	$2,883,000	**$1,715,000**	$1,548,000
Rental income	**2,041,000**	2,048,000	**1,672,000**	1,506,000
	$ 790,000	$ 835,000	**$ 43,000**	$ 42,000

Minimum future rental expense under commitments for noncancellable leases and minimum future rental income at November 30, 1975 are approximately as follows:

	Retail stores		Other leases	Rental income	Net commitment
	Subleased	Other			
Non-capitalized financing leases:					
Fiscal years:					
1976	$ 1,858,000	$ 811,000	$ 250,000	$ 2,105,000	$ 814,000
1977	1,843,000	811,000	179,000	2,086,000	747,000
1978	1,820,000	813,000	122,000	2,065,000	690,000
1979	1,773,000	816,000	73,000	2,022,000	640,000
1980	1,744,000	817,000	2,000	1,984,000	579,000
1981-1985	7,367,000	3,736,000	—	8,389,000	2,714,000
1986-1990	3,296,000	2,153,000	—	4,315,000	1,134,000
1991-1995	801,000	603,000	—	1,370,000	34,000
Thereafter	—	—	—	165,000	(165,000)
	$20,502,000	$10,560,000	$ 626,000	$24,501,000	$7,187,000
Non-financing leases:					
Fiscal years:					
1976	$ 503,000	$ 128,000	$ 471,000	$ 611,000	$ 491,000
1977	412,000	118,000	464,000	479,000	515,000
1978	356,000	113,000	453,000	408,000	514,000
1979	301,000	97,000	452,000	338,000	512,000
1980	217,000	72,000	452,000	253,000	488,000
1981-1985	325,000	204,000	2,024,000	458,000	2,095,000
1986-1990	55,000	72,000	85,000	8,000	204,000
1991-1995	42,000	—	—	—	42,000
	$ 2,211,000	$ 804,000	$4,401,000	$ 2,555,000	$4,861,000

The present value of the minimum rental commitments under non-capitalized financing leases at November 30, 1975 and 1974 and the present value of minimum future rental income are summarized below:

	1975	1974
Present value of rental commitments:		
Retail stores:		
Subleased	**$12,440,000**	$14,241,000
Other	**5,901,000**	5,660,000
Other leases	**524,000**	381,000
	18,865,000	20,282,000
Present value of future rental income	**13,474,000**	14,391,000
	$ 5,391,000	$ 5,891,000
Interest rates used in computing present value:		
Range	**5% to 18%**	5% to 18%
Weighted average	**9.1%**	8.9%

If all non-capitalized financing leases (including leases and sub-leases to franchise operators) had been capitalized, the related assets amortized on a straight-line basis and interest had been accrued on the basis of the outstanding principal balance, net income for fiscal 1975 and 1974 would have been reduced approximately as follows:

	1975	1974
Pro forma adjustments:		
Increase in interest expense	**$1,702,000**	$1,766,000
Increase in amortization	**505,000**	549,000
Increase in interest income	**(1,331,000)**	(1,364,000)
Decrease in rental income	**2,041,000**	2,048,000
Decrease in rental expense	**(2,831,000)**	(2,883,000)
Estimated income tax effect	**(22,000)**	—
Pro forma decrease in net income	**$ 64,000**	$ 116,000

In the ordinary course of business, the Company is subject to suits and claims by franchisees and others. The Company's management and legal counsel do not believe that the losses, if any, resulting from existing suits or claims would have a materially adverse effect on the consolidated financial statements.

7. Capital stock

Changes in capital stock and paid-in capital during fiscal 1974 and 1975 were as follows:

	7% Series B stock	Paid-in capital	Cost common treasury stock
Balance, November 30, 1973	$ —	$587,072	$349,965
Issue of 10,000 shares of common treasury stock for franchise rights	—	(21,239)	(41,239)
Issue of 5,706 shares of 7%, Series B stock to retire debt, net of related costs	57,060	(27,180)	—
Balance, November 30, 1974	57,060	538,653	308,726
Issue of 5,706 shares of 7%, Series B stock to retire debt, net of related costs	57,060	(27,179)	—
Balance, November 30, 1975	$114,120	$511,474	$308,726

There were no issues or retirements of common stock or 4%, Series A stock during fiscal 1974 and 1975.

The Company's Board of Directors is authorized to issue special preference stock, par value $10.00, in one or more series and to determine voting rights, dividend rates, redemption rights, convertibility and other preferences of each series. The Company's Board of Directors has reserved 450,000 shares of special preference stock designated as "Special 4% cumulative preferred stock, Series A" and 60,000 shares designated as "Special 7% cumulative preferred stock, Series B". Each share of Series A and Series B stock is convertible, at the option of the holder, into one share of common stock. The Series A stock is redeemable, at the Company's option, at par value plus accrued dividends. The Series B stock is redeemable, with certain limitations, at the option of the Company or the holder at par value plus accrued dividends.

Of the 4,854,682 shares of common stock authorized but unissued at November 30, 1975, 1,782,199 shares were reserved for issuance as follows:

Conversion of subordinated debentures, convertible at $1.50 per share	1,333,333
Conversion of special preference stock (see Note 5), convertible at $10.00 per share	112,816
Exercise of stock options (see Note 8)	336,050
	1,782,199

8. Stock options

The Company's qualified stock option plan provides for the granting of options for up to 300,000 shares of common stock to certain officers and key employees at not less than 100% of fair market value. Options are exercisable in four equal cumulative installments beginning one year from date of grant and expire in five years. No charges are made to income in accounting for options. Proceeds in excess of par value of the common stock are credited to paid-in capital.

During fiscal 1973, options for 142,300 shares ("replacement options") at $6.25 per share were granted to employees holding options for an equivalent number of shares at prices ranging from $8.25 to $20.00 and granted at various dates from 1971 to 1973. The replacement options expire five years from date of grant and may not be exercised while the prior option at a higher price is outstanding.

At November 30, 1974, options for 197,625 shares were outstanding under the plan at prices ranging from $1.63 to $20.00 per share (excluding replacement options), of which options for 105,500 shares were exercisable, and 85,925 shares were available for granting of options. During fiscal 1975, options for 19,500 shares were granted at prices ranging from $2.00 to $2.88 per share and options for 18,625 shares were cancelled because of terminations of employment. At November 30, 1975, options for 198,500 shares were outstanding (excluding replacement options) at prices ranging from $1.63 to $20.00 per share, of which options for 148,000 shares were exercisable, and 85,050 shares were available for granting of options.

During fiscal 1975, the Company granted non-qualified stock options to certain officers for a total of 52,500 shares of common stock at $1.75 per share, the market value at date of grant. The options are exercisable at any time, in whole or in part, and expire five years after the date of grant.

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

The Board of Directors and Stockholders
International Dairy Queen, Inc.

We have examined the accompanying consolidated balance sheet of International Dairy Queen, Inc. at November 30, 1975 and the related consolidated statements of income and retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We have previously made a similar examination of the financial statements for the prior year.

In our opinion, the statements mentioned above present fairly the consolidated financial position of International Dairy Queen, Inc. at November 30, 1975 and 1974 and the consolidated results of operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis during the period.

ARTHUR YOUNG & COMPANY

Minneapolis, Minnesota
January 15, 1976

CORPORATE DIRECTORY

BOARD OF DIRECTORS

*HARRIS COOPER	*President and Chief Executive and Chief Operating Officer of the Company*
JAMES C. CRUIKSHANK	*Private investor*
ERNEST F. DORN	*Chairman of the Board of Directors of Community Credit Co.*
*RUDY LUTHER	*President of Hansord Pontiac Company*
W. DUNCAN MacMILLAN	*President of Waycrosse, Inc., a company which is primarily engaged in the manufacture of farm equipment and the design, fabrication and installation of fire protection systems.*
*W. B. McKINSTRY	*Chairman of the Board of Directors and Executive Committee of the Company and private investor*
RAYMOND MITHUN	*Founder-Chairman of Campbell-Mithun, Inc. and President of Mithun Enterprises, Inc., both companies are engaged either directly or indirectly in the advertising business.*
JANE N. MOOTY	*Private Investor*
*JOHN W. MOOTY	*Secretary of the Company; Partner in the Minneapolis law firm of Gray, Plant, Mooty & Anderson*
RAYMOND SCHWEIGERT	*President of Schweigert Meat Co.*

*Member of Executive Committee

OFFICERS

W. B. McKINSTRY	*Chairman of the Board and Chairman of the Executive Committee*
HARRIS COOPER	*President and Chief Executive and Chief Operating Officer*
GORDON F. HUBER	*Executive Vice President—Operations*
GLENN H. MUEFFELMANN	*Executive Vice President—Finance and Assistant Secretary*
EDWARD P. GHERITY	*Vice President—Purchasing*
JOHN HANNING	*Vice President—Corporate Store Development*
FRANK HEIT	*Treasurer*
DONALD R. HERBECK	*Vice President—International Division and Franchise Development*
JOHN W. MOOTY	*Secretary*
HERMAN E. NELSON	*Vice President—Law and Assistant Secretary*
RICHARD D. STANTON	*Vice President—Equipment*
JOHN T. STORK	*Vice President—Food Products Division*

ANNUAL MEETING

The annual meeting of shareholders will be held Tuesday, March 2, 1976, at 11:00 a.m. in the General Offices of the Company.

FORM 10-K

A copy of the annual report to the Securities and Exchange Commission (Form 10-K) can be obtained by writing to the Company.

GENERAL OFFICES
International Dairy Queen, Inc.
5701 Green Valley Drive
Minneapolis, Minnesota 55437
(612) 835-3700

AUDITORS
Arthur Young & Company
Minneapolis, Minnesota 55402

COUNSEL
Gray, Plant, Mooty & Anderson
Minneapolis, Minnesota 55402

REGISTRAR
Northwestern National Bank
of Minneapolis, 55480

TRANSFER AGENT
Northwestern National Bank
of Minneapolis, 55480

STOCK DATA
Traded on the National Over-the-Counter Market

NASDAQ SYMBOL:
INDQ

PRICE RANGE OF COMMON STOCK

The high and low bid prices for the Company's common stock in the over-the-counter market for the periods shown, as reported by the Wall Street Journal, are as indicated below:

PERIOD—FISCAL YEAR 1974	Low Bid	High Bid
First Quarter	2	4¼
Second Quarter	2¾	4
Third Quarter	2	2¾
Fourth Quarter	1	2¼

PERIOD—FISCAL YEAR 1975	Low Bid	High Bid
First Quarter	1⅛	2
Second Quarter	1¾	2⅝
Third Quarter	1⅝	2¼
Fourth Quarter	1⅜	2¼

Dividends have not been paid on common stock.

INTERNATIONAL DAIRY QUEEN, INC.

FINANCIAL SUMMARY

(Dollars in thousands except shares and per share data)

	1975	1974	1973	1972	1971
OPERATIONS:					
(Fiscal year ended November 30)					
Revenues:					
Net sales:					
Food and supplies	**$27,992**	$25,907	$23,923	$20,186	$21,593
Equipment	**2,986**	3,953	3,046	2,724	1,782
Mix and concentrates	**4,100**	4,213	3,870	4,298	4,822
Other	**1,749**	2,000	2,505	2,795	1,591
	36,827	36,073	33,344	30,003	29,788
Service fees	**9,212**	8,431	7,541	6,418	6,134
Franchise sales and other fees	**2,926**	2,716	2,374	2,124	1,323
Real estate rentals	**4,065**	3,846	3,557	3,353	3,265
Other	**1,471**	1,575	1,714	1,406	710
	54,501	52,641	48,530	43,304	41,220
Costs and expenses:					
Cost of sales	**33,394**	32,358	30,188	26,688	26,858
Expenses applicable to real estate rentals	**3,564**	3,470	3,328	3,135	3,109
Selling, general and administrative	**13,672**	12,908	11,899	10,094	8,187
Interest	**2,268**	2,782	2,157	1,352	1,179
	52,898	51,518	47,572	41,269	39,333
Income before income taxes and extraordinary items	**1,603**	1,123	958	2,035	1,887
Provision for income taxes	**595**	305	261	760	837
Income before extraordinary items	**1,008**	818	697	1,275	1,050
Extraordinary items	**—**	—	—	101	657
Net income	**$ 1,008**	$ 818	$ 697	$ 1,376	$ 1,707
Net income per common share	**$ .17**	$ .15	$ .12	$ .22	$ .29
Average common and common equivalent shares outstanding	**6,392,584**	6,389,201	6,291,589	6,315,170	5,889,681
FINANCIAL CONDITION:					
(At fiscal year end)					
Total assets	**$43,266**	$43,710	$42,036	$38,584	$33,650
Long term debt	**20,217**	23,503	23,423	20,705	18,245
Stockholders' equity	**11,420**	10,411	9,571	8,451	6,920

Quarterly Data:	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
1975	**$(994)**	**$814**	**$1,407**	**$(219)**
1974	(757)	461	1,246	(132)